Talk to Rotarians

- I -

As you are probably all aware an economic topic requires very much more time than the time made available at one of our Luncheons. I have however, chosen to give a talk on inflation; the welfare aspects of inflation and the socio economic effects and consequences without getting too technical. I shall also endeavour to relate certain of these aspects to the South African economy in view of the very serious inflationary trends in our midst, together with a brief examination as to why the authorities have possibly been in my opinion so hesitant in attempting to curb inflation. Please take note that I have used the term " curb inflation" and not deflation. This is simply in view of the fact that the government is well aware of the peculiarities of the South African Economy and that it would not take much in an deflationary tendency to create doom rather than boom for us in South Africa.

Although, it may be argued that inflation is currently and has been for a decade or more and threatens to be in the future one of the most crucial problems for most countries in the world I must however mention that Lenin was said to have declared the best way to destroy the capitalist system was to debauch the currency. This gentlemen is what is happening at present not only in South Africa but throughout all the capitalist economies of the world.

It does seem that prices will continue to rise as far as human wisdom can see ahead. A creeping inflation of approximately 2% p.a. has been a natural tendency and what one might add a necessary aspect to put a bit of fire into the business mans expectations. This gentlemen is one of the main reasons why the entrepreneus tends to manufacture or hold stocks in expectation of demand. We cannot imagine this being practical if there was a tendency for prices to drop continuously and from time to time.

This...../2

This factor of creeping inflation was always accepted as something normal. 2% p.a. does not seem on the face of it to be a damaging figure, but in recent times where this figure has been more than doubled even our financial institutions have had to take heed and do something. A good example of this is our insurance companies at present in South Africa. They are introducing methods whereby the value of ones expected monetary return on an insurance policy is augmented to such a degree that the loss in value of money at the future date of receipt would not have dwindled to a useless amount from its purchasing power aspect. They are participating in the Unit Trust movement in order to achieve this.

At this stage however, I wish to emphasise that inflation is not the mere rise in prices which we are experiencing today but it may be defined as to much money chasing to few goods and hence rising prices are merely a sympton of it.

Indeed, in same instances price rises are deflationary ~~in some instances~~. For example if the cost of certain products in normal conditions rises to such an extent that it becomes out of the reach of its usual purchasers the demand will drop and hence that particular industry will have to supply less of the products and so possible retrenchment etc. might occur in that particular industry.

South Africa in these times is said to be undergoing a demand inflation ! That is there is a greater demand for products than what the economy can satisfy under present product conditions South Africa's present productive resources have become exhausted to a certain extent. For example we are all aware of the scarcity of labour both skilled and unskilled. Hence entrepreneus in order to attempt to satisfy demand are paying higher labour prices and so the price of the product is increased, and here I need not go any further as the cycle of rising prices caused by

the &c...../.3

have to be replaced, thus the continuous demand for more arms is inflationary due to the drain on industry and not being able to shift to other lines. This cold war factor, I must emphasise is most inflationary during conditions such as these today - namely full employment.

On the other hand gentlemen not one of us will deny that this armament policy was the original injection required after the Sharpville crisis to start the economy on the upward trend.

Secondly the strength of trade unions. Trade Unions are becomimg stronger in all the Free countries. In particular rising prices are drawing more and more salaried workers into Unions. Again here full employment is the main cause - full employment a policy towards which nearly every Government in the world is committed. Only an intolerable degree of unemployment could keep modern trade unions in order.

This coupled with the fact that democratic countries are tending to shift to the left makes one have to accept the sacrosanctity of full employment. Capitalist countries are tending

these conditions of "full employment", we have unfortunately all been made aware of. We see here in simple language productivity is not being increased but prices are.

Let us look at the reasons briefly as to why we have inflation. What are the forces and causes of full employment, which leads to greater demand for products which the economy cannot at present satisfy.

Firstly, War and the Cold War. Even South Africa today is participating in the cold war. Indeed not one of us will argue that we have only in recent years being made aware of the true armamentp policy being undertaken by the present government. The same obviously undoubtedly applies to each and every other economy. Preparation for an expected war seems to have become part and parcel of our lives. But, to make it worse we find that these weapons become obsolete inspite of them not being used and hence

regarded today as an essentually a right wing measure and even more important it is felt "undemocratic", to cause deflation and hence unemployment. It is very much easier to grant wage claims, tariffs or a subsidy in order to level up incomes of those who have fallen behind than to cut the money incomes of everyone else back to the old level, though in the long run the effect on real incomes is the same.

To quote the London Economist "The Century of the Common Man is no time for orthodox finance and furthermore no government will cut its own throat on monetary grounds even though the seriousness of the inflation is realised".

Thirdly - the desirability of cheap money under all circumstances and the implication that internal prosperity can be achieved without reference to international trade are all misleading and in effect inflationary.

Fourthly - again referring to the welfare tendencies - namely social services provided by authorities - this causes an inexaustible drain upon the government purse. We know the government tries to spend more and tax less, so that the poor may may be helped and thus making it difficult to balance the budget, inflationary policy.

Fifthly - There are a number of highly inflationary international tendencies. The first of these is the end of free trade. Protection always has an inflationary effect at the moment when it is imposed - for it raises the price of certain imports and stimulates the demand for import substitutes - This gentlemen is very well provided the local industries play the game.

Let us examine our industries in South Africa.-Protection is offered to young industries in order to enable them to find their feet and be able to provide a product at a price acceptable to all and also to enable it to become competitive on the international plain - but instead, under the cloak of protection we find that the industry tends to profiteering rather than utilizing the

opportunity afforded to increase the efficiency of their productivity. In other words we come back to the old phrase to quote - "Our baby industries never seem to grow up." Thus having defeated as we can see the initial objects of government protection but yet the stigma of the price increase having been left. It takes time for the authorities to become aware of such motives and when discovered, the damage has already been done.

Sixth to quote the London Economist - In the past if a country through inflation or any other cause was running an unfavourable balance of payments it had to stand on its own feet in the end and check the outflow by deflation. Since the last war however, inflation has been floated off by some form of intergovernmental charity, an example of this is the Marshall Aid or the Colombo plan in India, thus the unfavourable trade balance to quote is "usually met by a kind of fairy from without and the spending spree may continue from within the country. We must also bear in mind however, that due to this charity work by her country the fairy causes inflation in her own country.

I here agree with the London Economist that we seem to be flowing from the welfare state into the welfare world. Incomes are not equalised from within but also between nations and this depresses the rate of world savings atill further.

We know that requests are made by the South African Government to save more and spend less, but, this is very difficult for the average man to accept and also to be able to do. The lower income group simply cannot save because they are already finding matters beyond their means let alone have a surplus in monetary income.

The richer group - what problems are they facing, apart from the fact that surplus liquidity is being drained by "fiscal policy" i.e. the so called credit squeeze in order to try and curb the demand inflation of the economy which previously referred to as

the type...../6

the type of inflation South Africa is facing. This man has lost or is beginning to loose confidence in cash. He feels that by placing for example money on fixed deposit the difference between the tax level and the rate of interest is most discouraging indeed and hence he rather places his money in capital objects such as fixed property, where he can hedge against any form of monetary loss due to the present inflationary trend.

Therefore gentlemen we can see that the so called profiteers "are a consequence and not a cause of rising prices", But I also agree and admit that the "process of wealth-getting in this manner degenerates into a gamble and a lottery" which is very dangerous indeed at any time.

South Africa has the weapons to curb the inflation which I feel confident is going to achieve in the immediate future. But she cannot be too harsh for we must accept the policy adopted of "Social security rather than economic progress and stability".

South Africa had to istall confidence into the economy, especially after the Sharpville crisis, This was managed and we saw the South African trade cycle swing upwards, reserves rising etc. at the same time the Social Policy of immigration was adopted which added even greater impetus to the economy and it was not long before before we realised that we simply could not meet the demand in any productivity asked for, for reasons already discussed.

What must South Africa do - stop immigration and so arrest demand to a certain degree or adopt a strong deflationary ~~policy~~ policy and cause a bit of unemployment. Will this be acceptable - I think not.

Let us face it gentlemen we are all employed in one respect or another - Would we like to be unemployed for a short period knowing that it is for our own good in the long run or would we rather

accept ...../7.

accept the catastrophe of inflation and continue as we are although the long term effect will be worse - I think not - not anyone of us would like to see himself unemployed for any period of time. Hence we can see the difficulty of the authorities who at the same time must be careful not to destroy the economic confidence in the country but at the same time would not like to cause social unrest amongst its peoples - as unlike other countries - we are aware of the racial "national structure of the country and this no lightweight hanging over anybodys' head. Hence gentlemen I think we can appreciate the difficulties the authorities are facing at the moment simply because touch the economic structure too harshly - the social structure gives trouble - play with the social structure to achieve the economic stability we so much want a very very difficult decision to take in a country such as ours.